No. 88-1951

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In The

Supreme Court of the United States

October Term, 1989

UNITED STATES OF AMERICA

Petitioner,

v.

FRANCES L. DALM

Respondent.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SIXTH CIRCUIT

BRIEF FOR THE RESPONDENT

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QUESTION PRESENTED

Where the Government has asserted a timely income tax deficiency against Taxpayer and, as a result two taxes have been collected on the same taxable event on mutually exclusive theories, does equitable recoupment permit the Taxpayer to maintain a suit against the Government to reduce the amount received by the Government?

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CORRECTION TO PETITIONER'S STATEMENT OF THE CASE

Prior to the Tax Court's Decision on December 4, 1984, Respondent's claim for refund was filed November 1, 1984. (See C.A. App. 7, 9) As the claim was filed in recoupment against a timely claim of the Government, the claim was timely. The Government's assertion that the claim was untimely and that suit is otherwise barred as untimely by Sections 7422 and 6511 of the Internal Revenue Code are not statements of fact but their conclusions of law.

The Government draws conclusions from use of the words "payment," "paid the reported gift tax," "claim was untimely," and "the suit unquestionably was untimely." A more accurate statement is that "Respondent received from Clarence . . . " monies in the amounts stated and that "Respondent sent a check to the Internal Revenue Service in 1976 which was intended to pay the reported gift tax of $18,675."

The above distinction is material only because of the Government's repetitive conclusions of "untimely" which are utterly inconsistent with its position that the transfers in question were income in which case there was no gift, no gift tax return required and hence no gift tax. It therefore follows under the Government's logic that the gift tax was not paid in 1976 within the strict meaning of Section 6511 of the Internal Revenue Code. Hence, the two (2) year period did not begin to run in 1976 and the suit was timely.

Moreover a forthright statement should include the Government's implicit admission that the essential elements of equitable recoupment mandated by *Bull v.*

United States, 295 U.S. 247 (1935), *Stone v. White*, 301 U.S. 532 (1937) and *Rothensies v. Electric Storage Battery*, 329 U.S. 296 (1946) are present in *Dalm*.

SUMMARY OF ARGUMENT

The only distinction between *Bull* and *Dalm* is a meaningless procedural distinction which, if dispositive, would have rendered the *Bull* decision obsolete upon issuance, contrary to the philosophy behind adjudication by the Supreme Court.

Equitable recoupment requires that a single transaction be subjected to two taxes on inconsistent legal theories. In *Dalm* it was the identical receipt of money. The right to recoupment does not arise until the second tax is collected. The erroneous tax is not "erroneously paid" until the second tax is collected. Therefore it is unnecessary for the Plaintiff to show that her suit was "timely" as the term is used by the Government.

The point that the Government refuses to recognize is that the taxpayer had no action to bring with respect to the "erroneously paid" gift tax and overpaid income tax until the Settlement and Tax Court decision determined that an income tax would be collected. If the IRS had properly credited the gift tax payment against the amount of income tax which was due, then no action would have been necessary. It was only after the Revenue Service determined that the income tax was due without giving credit for the tax already paid on the transaction that the doctrine of equitable recoupment became applicable. Therefore, pursuant to the doctrine of equitable

recoupment, Respondent's action survives as long as the Government's action survives against her. Furthermore, the defense of sovereign immunity was waived by the Government when it proceeded against the Respondent for $160,000 additional income tax.

Respondent's action was not an "independent" action as that term has been defined by the cases. An "independent action" is that which does not seek to recoup a claim against the amount of a properly asserted and timely deficiency. The Taxpayer's action arises because the Government asserted a timely deficiency.

A correct reading of *Bull* indicates that the Government's assertion of a deficiency is the "main action" which must be timely to allow a claim of recoupment. None of the cases cited by the Government present a situation in which recoupment was not allowed when two taxes have been collected on the same identical taxable event and the Government has asserted a timely deficiency. All of the prior cases cited in *Bull* support this interpretation of the Court's reasoning. A recoupment claim survives as long as the claim opposing it without regard to how the party asserting the main claim proceeds.

The legislative history of the mitigation provisions reveal that these provisions deal with income tax alone and were meant to complement and not replace equitable recoupment.

In conclusion, the Court of Appeals holding in *Dalm* is consistent with the philosophical theory underlying statutes of limitations. No stale claims are involved. The Tax Court decision as to whether the sums involved were

income was equally dispositive as to whether they were gifts. The Government decided to litigate the one claim, and the determination as to the one was automatically determinative of the other and those conclusions already reached mandate a refund to the Taxpayer.

I. THE *DALM* CASE IS IDENTICAL IN ALL SUBSTANTIVE RESPECTS TO *BULL V. UNITED STATES*

The foundation of the doctrine of equitable recoupment as applied to Federal tax cases was, as both sides agree, *Bull v. United States*, 295 U.S. 247 (1935). If it is held that Plaintiff Frances Dalm's situation is, in substance, that of the Plaintiff Estate in *Bull*, Plaintiff (Respondent) should prevail.

In both *Bull* and *Dalm*, the Taxpayer voluntarily paid a non-income tax (in *Bull*, Estate Tax and in *Dalm*, Gift Tax). In both cases, the Government then asserted a deficiency in income tax, a deficiency the Taxpayer opposed in the Tax Court (Board of Tax Appeals in *Bull*). Both taxpayers were held to owe income tax, which was then paid. Both then filed suits for refund.

The Government argues that in *Bull* the properly owed tax (the income tax) was still subject to a suit for refund and it was as a credit against the proper income tax that the improper estate tax was recouped. *Bull* was decided in 1935 but involved a tax year prior to 1926 when the decisions of the Board of Tax Appeals were not conclusive whereas, the Revenue Act of 1926 made decisions of the Board of Tax Appeals final. Accordingly, it must be concluded, if such a distinction is controlling,

that this court formulated a fundamentally fair doctrine in 1935 in a situation which, due to the change of statute, would never occur again. Respondent therefore respectfully submits that in order for the Court to hold in favor of the Government, it must also be concluded that the Supreme Court decreed an equitable doctrine in a situation where it was against morality and conscience for a certain result to occur and then placed prerequisites in its Opinion to assure the doctrine would never be used in precisely the same way again. Such a conclusion places the Court on a lower plane and ignores the role of the Supreme Court which is not only to rectify injustices in particular instances but to provide guidance for the jurisprudence of the nation.

Part of the controversy is generated by the meaning of the term "recoupment." Obviously, more is required than that an otherwise valid claim be barred by the Statute of Limitations. More is required than that the Government have a valid claim against the Taxpayer against which the Taxpayer can set off its barred claim against the Government. What is required is that the two claims be so intimately related that the decision as to one results almost automatically in the decision as to the other. As set forth in *Rothensies v. Electric Storage Battery Co.*, 329 U.S. 296, 299-300, (1946) referring to *Bull* and *Stone*:

> "In both cases a single transaction constituted the taxable event claimed upon and the one considered in recoupment. In both, the single transaction or taxable event had been subjected to two taxes on inconsistent legal theories, and what was mistakenly paid was recouped against what was correctly due."

A single transaction and a single taxable event must be involved and must be examined "in all of its aspects" in order to render judgment that does justice in view of the transaction as a whole, *Dalm v. United States*, Pet. App. 9a citing *Electric Storage Battery*, at 299. Once it is determined that a tax is owing on a single transaction which transaction has been subjected to a prior tax on an inconsistent legal theory automatically and only at the instant the proper tax is determined, the previously collected tax may be recouped against the properly owed tax. In effect, the improper tax becomes paid only at that point because only then have facts been determined to support the conclusion it was improperly paid. From that point on (the final determination of the proper tax) the Taxpayer has two years to seek a refund. A correct tax having been determined and paid, there is now a fund to recoup against. The recoupable portion of the properly payable tax has become available and should be instantly refunded. In *Dalm* administrative remedies were exhausted by filing the claim for refund which Respondent mistakenly anticipated would be forthcoming. Therefore, a suit for refund in the District Court is available and was the proper remedy.

II. TAXPAYER'S ACTION WAS TIMELY

Heretofore, the Respondent has not sought to show that her suit was timely in that the cases are clear that it is the action of the Government that must be timely. It is undisputed that the action of the Government in this case, its determination that Respondent owed an income tax, not a gift tax, was timely.

In fact, the Respondent's action has been timely because the gift tax only became refundable upon the payment of income tax on the same sum of money because then and only then was the gift tax overpaid. For the entire period from 1976 to 1984, only one improper tax had been collected on the transaction in question, the gift tax. There was no cause to seek a refund of such tax because the only possible justification for claiming that a gift tax was not owed was that the transaction was not a gift. However, when it was determined that income tax was owed on the transaction, *then and only then* was the gift tax refundable. The Dalms' action therefore was properly filed within two years.

Periods of limitations generally are triggered by the accrual of the cause of action. An action generally accrues at the time the last event rendering the cause of action complete occurs. In most tax cases, the cause of action becomes complete at the time the tax is paid. However, in a case requiring the application of equitable recoupment, the cause of action is rendered complete by a second tax being collected on the same fund of money as respects the same party in the same transaction. Accordingly, the improper tax in *Dalm* was only paid at the time (1984) when the payment of the proper tax rendered the original payments improper. Otherwise, the statute of Limitations will have expired on an inchoate cause of action before the cause of action has arisen. Thus, the claim should be considered timely within the meaning of Section 6511 of the Internal Revenue Code. Judge Learned Hand's observation in *Elbert v. Johnson*, 164 F.2d 421 (2nd Cir. 1947) at 425-426 is apposite despite the Government's inaccurate paraphrasing and erroneous statement, (at page 8 of its

Brief In Reply to Respondent's Brief opposing the Petition for *Certiorari*), that the language in *Bull* contradicted such statement. The Government changed Hand's word, "assert" to "litigate" and failed to inform this Court that the language from *Bull* was taken out of context. Judge Hand cogently stated:

> "That decision (*Bull*), as I understand it, permits a taxpayer without penalty to assert his version of a transaction, until it is finally decided against him. That is to say, if the transaction, is susceptible of two interpretations, and the taxpayer has paid a tax which was required by the interpretation he puts upon it, he does not forfeit his right to a refund of that tax, because the statute of limitation has run against him before the Courts have finally decided that his interpretation was wrong; the statute is tolled."

The claim for refund did not arise *ab initio* upon the payment in 1976 on the ground that the gift tax was improperly paid. The action for refund of the gift tax arose because an income tax has been determined and collected and the income tax was not collected until 1984.

Despite its inconsistency as pointed out in the Correction to Statement, the Government argues that the statutory scheme constitutes an exception to sovereign immunity and, as such, the statutes must be strictly construed. In effect, the Government states the sovereign need not have consented to be sued at all and therefore it does not matter how unfair the statutory scheme is. The sovereign cannot fail to allow due process in the suits it allows against itself because the conditions Congress places on its consent for the sovereign to be sued must be constitutional. See *Deakyne v. Department of Army Corps of*

Engineers, 701 F.2d 271, 174 (3rd Cir. 1983). It could hardly be argued that Congress could limit an action to members of one race or religion. An action that is barred by the Statute of Limitations before it accrues is a violation of due process because there has been no fair opportunity to be heard. See *Logan v. Zimmerman Brush Company*, 455 U.S. 422, 429, 71 L.Ed.2d 265, 102 S. Ct. 1148 (1982) and the cases cited therein. The Government's emphasis on absolute sovereign immunity makes one think we live under a monarchy rather than our beloved republic.

Further, the Government has waived any sovereign immunity by bringing an action against the Dalms for additional income tax.

> "The general rule is that when the sovereign sues, it waives immunity as to claims of the Defendant which assert matters in recoupment arising out of the same transaction or occurrence which is the subject matter of the Government's suit and to the extent of defeating the Government's claim but not to the extent of a judgment against the Government which is affirmative in the sense of involving relief different in kind or nature to that sought by the Government or in the sense of exceeding the amount of the Government's claims . . . " *U.S. v. Johnson*, 853 F.2d 619 (8th Cir. 1988) citing *Frederick v. United States*, 386 F.2d 481, 488 (5th Cir. 1967)

The Government, by asserting a deficiency for additional income tax has opened itself up to claims of recoupment against that deficiency. Respondent has used recoupment "in the nature of a defense" (*Bull* at 262) and her claim cannot be barred as long as the Government's claim is not barred.

III. TAXPAYER'S ACTION WAS NOT INDEPENDENT

After the initial cases of *Bull* and *Stone*, this Court defined the essence of the doctrine of equitable recoupment as preventing the collection of two inconsistent taxes on the same receipt of funds by the same Taxpayer.

The Court of Appeals in *Dalm* was absolutely correct in stating that: "The facts in *Rothensies v. Electric Storage Battery* were quite different from those in *Bull* and the present case." The Special Assistant to the Attorney General who argued the *Electric Storage Battery* case pointed out that recovery in that case would not be supported upon equitable principles of recoupment and more importantly that *Bull* was inapplicable because the barred excise taxes did not arise out of the same transaction as the income taxes. While the Taxpayer's suit for refund in *Electric Storage Battery* was conceded as timely, the claim pleaded as a recoupment was for taxes collected over twenty (20) years before on completely different transactions than the transactions on which the tax had properly been paid. There was no single taxable event that had been subjected to two taxes on inconsistent legal theories. *Bull*, *Stone*, the *Dalm* case, and *Electric Storage Battery* are consistent. All stand for the proposition that the doctrine of equitable recoupment is applicable only where a single taxable event and single transaction has been subjected to two taxes on inconsistent legal theories. However, in *O'Brien v. United States*, 766 F.2d 1038 (7th Cir. 1985), *Electric Storage Battery* and the other cases cited by the Government, the doctrine correctly should not have been applied and was not. It should be emphasized that in *Electric Storage Battery*, no issue was involved regarding

the suit for refund being timely but recoupment was still improper because the taxes did not involve a single transaction.

The Government makes much ado over whether an action is "independent" with the frequent admonition that the doctrine of equitable recoupment does not permit an independent action. Respondent submits, however that "independent" has a rather specialized meaning in this context. An "independent" action is an action that does not follow a timely assertion of a deficiency on the part of the Government.

Dalm is not *an independent suit* as the Seventh Circuit in *O'Brien* defined one because the deficiency for additional income tax asserted by the Government against Frances Dalm was timely. In *O'Brien*, at page 1049, it is stated "O'Brien's untimely refund suit in 1983 asserts recoupment affirmatively to recover an erroneously paid tax and does not seek to offset the amount of a properly asserted and timely deficiency." The Court concluded that *"This Court sees no grounds for extending the doctrine and the Plaintiff offers none"* for the very reason that the Plaintiff was not seeking an offset against a properly asserted and timely deficiency. The *Dalm* suit, likewise, because recoupment is sought by the proper person against a properly owed tax paid by the same Taxpayer, pursuant to the stipulated Order of the Tax Court after the government's timely assertion of a deficiency, is not an independent action as the Seventh Circuit uses the term.

The Court in *Bull* discussed at length the nature of tax litigation, explaining that tax litigation is essentially an action for debt with the order of events reversed because the sovereign is the Creditor. Instead of a suit for debt followed by collection, in the case of a tax suit, the collection comes first.

> "If the claim for income tax deficiency had been the subject of a suit, any counter demand for recoupment of the overpayment of estate tax could have been asserted by way of defense and credit obtained notwithstanding the Statute of Limitations had barred an independent suit against the Government therefor." *Bull* at 262

The Court further stated:

> "In a proceeding for the collection of estate tax, the United States through a palpable mistake took more than it was entitled to. Retention of the money was against morality and conscience. But claim for refund or credit was not presented or action instituted for restitution within the period fixed by the Statute of Limitations. *If nothing further had occurred Congressional action would have been the sole avenue of redress." Id.* 260-261

But something further did happen as described by the Court in the very next line, "In July, 1925, the Government brought a new proceeding arising out of the same transaction involved in the earlier proceeding." Thus, the Government asserting a timely deficiency of income tax is what revitalized the claim for Estate Tax. In the present case, as in *Bull*, if the Government had not brought an action for the income tax deficiency and the statute of limitations expired on the gift tax claim, then the gift tax

could not have been questioned. The statute of limitations would have barred the claim, but since the Government sought to collect a different tax on the same transaction, the Dalms have the right under equitable recoupment to reduce the net amount collected by the Government.

The doctrine of equitable recoupment could not be raised and was irrelevant to the issues before the Tax Court in *Dalm* as the Government agrees. Now that the action has moved to the District Court and involves a matter of collection the doctrine of equitable recoupment becomes relevant to defend the Dalms against the collection of the wrong amount of tax.

The Government has cited three separate cases for the proposition that the doctrine of equitable recoupment did not allow the institution of an "independent" suit. All of such cases are distinguishable from the case at bar. In none of these cases did the suit follow the timely assertion by the Government of a deficiency. Moreover, the Government's reliance on such cases is misplaced because the cases did not contain the essential elements of equitable recoupment.

In *Brigham v. United States*, 470 F.2d 571 (Ct. Cl. 1972) *cert. denied*, 414 U.S. 831 (1973) the Taxpayer had sold stock on an installment basis and reported the installments as capital gains for the taxable years 1958-1961. The returns were examined, the installments reclassified as ordinary income, and the Taxpayers paid the determined deficiencies. Subsequently, the Supreme Court decided in a similar case that the original capital gains treatment had been correct. The Taxpayers sought

refunds for the income tax they had "erroneously paid." There was no deficiency against which to recoup such refunds. Neither were two different taxes collected on the same transaction. Only one tax was collected. The Taxpayers could have litigated the question, did not, and then, finding they would have won, regretted it.

No deficiency was collected by the Government on a receipt of money by the Taxpayer on which tax had already been paid on an inconsistent theory. It was acknowledged by both parties that the receipt was income. The Taxpayers had merely been incorrectly deprived of the capital gains exclusion in the barred years. Not only was the Taxpayers' action totally "independent" in every sense of the word but the facts did not contain the essential elements giving rise to equitable recoupment.

Respondent never had the opportunity or necessity to question the correctness of the gift tax payment until the Government asserted the transfer of money was additional income on which income tax was due. The finding that the receipt was income automatically (and for the first time) made the gift tax payment wrong. There was no equivalent event in *Brigham*. The receipt of income had been in years and with regard to transactions that the Government had made no move to revisit.

Evans Trust v. United States, 462 F.2d 521 (Ct. Cl. 1972) involved a Trust that had in years past, paid income tax on the receipt of installment payments from certain notes. The deceased trust beneficiary (the Estate) undervalued property in its estate tax return. The terms of the Tax

Court settlement were that there was no deficiency in estate tax but that the notes should be included in the estate thereby resulting in income in respect of a decedent.

The Trust had not been a party to the Tax Court litigation nor had any deficiency been determined as a result of the Tax Court action. No deficiency had ever been asserted against the Taxpayer trust and certainly no deficiency based on treating a receipt of money on which tax had already been paid as taxable on an inconsistent theory. A "new" tax had become payable, resulting in a theoretical "deduction" that could not be taken because the years were closed. This is entirely different from a second tax being collected on payments on an inconsistent theory against which the first tax should be credited. The relationship was so abstract that it took the interested parties six months after the settlement to realize that the revised tax treatment for the Estate might give rise to a deduction for a related Taxpayer, the Trust. During that time, the Statute expired on one of the tax years involved. The Dalms' claim required no extended analysis. If the money was income, it was not a gift which conclusion was axiomatic and elementary as evidenced by the immediate claim for refund prior to the Tax Court's decision becoming final.

Ellard v. United States, 228 Ct. Cl. 815 (1981) is even more different. Indeed, the Government had assessed no deficiency against the Taxpayer for him to recoup the taxes against. It concerned excise taxes paid on fuel sold

for highway use. An individual sold the fuel to a partnership and paid excise taxes on the sale. The partnership sold it to the public and did not pay excise taxes. The Government asserted a deficiency against the partnership, *which the partnership was still contesting* at the time of the suit for refund by the individual. Two separate transactions were involved, and accordingly, the test of *Rothensies v. Electric Storage Battery* was not met.

An action is not "independent" if the "main action" is timely. See *Bull* at 262. The Government has wrongly implied that the "main action" which must be timely is the Taxpayer's action. In *O'Brien*, it is clear that the "main action" that had to be timely was the government's assertion of a deficiency and not the Taxpayer's claim for refund. The *O'Brien* court recognized the distinction in stating at page 1049 that the doctrine will "permit a taxpayer to recoup an erroneously paid tax, the refund of which is time barred, against a timely and correctly asserted deficiency by the government." In fact, later on in its opinion, the Court set forth an instance in which equitable recoupment *perhaps could* have applied as follows:

> "The estate potentially could have recouped Michael O'Brien's income tax overpayment against the excess estate tax owed by the estate *resulting from the Tax Court's stipulated order.* Assertion of the doctrine would be proper because the 'main action,' the government's deficiency suit, would be timely." (emphasis added) *O'Brien* at 1050.

Interestingly enough, the Court's precise language is applicable to the present case as follows:

> "Dalm could recoup her gift tax overpayment against the excess income tax resulting from the Tax Court's stipulated Order, assertion of the doctrine . . . "

However, even were the above not compelling enough, what the Court in *Bull* meant by the "main action" can be determined by referring to the eight cases cited by the Court for its proposition. In every one of the cases cited by the Court, the "main action" is that brought by the opponent of the party with the recoupment claim.[1]

The theory upon which the Court based it decision is well exemplified by this statement in *Williams* at 13:

> "The defense of reduction or recoupment which arises out of the same transaction as the Note or claim survives as long as the cause of action upon the note or claim exists, although an affirmative action upon the subject of it may be barred by the Statute of Limitations."

In the present case, Dalms' claim for Refund was filed November 1, 1984 *before* the decision was entered in the Tax Court Case (December 4, 1984) and well before that decision was final. The main claim surviving, so did

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[1] *Blackshear v. Dekle*, 120 Ga. 766; 48 S.E. 311 (1904); *Aultman & Co. v. Torrey*, 55 Minn. 492; 57 N.W. 211 (1893); *Kaup v. Schinstock*, 88 Neb. 95; 129 N.W. 184 (1910) and *Campbell v. Hughes*, 73 Hun. (N.Y.) 14, 25 N.Y.S. 1021 (1893); *Williams v. Neely*, 134 Fed. 1 (8th Cir. 1904); *Conner v. Smith*, 88 Ala. 300, 7 So. 150 (1889); *Stewart v. Simon*, 111 Ark. 358, 163 S.W. 1135 (1914); *Beecher v. Baldwin*, 55 Conn. 419 (1887).

the recoupment claim. The Tax Court had no jurisdiction over a gift tax claim (there was no deficiency in gift tax to invoke such jurisdiction) but the District Court did. Taxpayer properly proceeded.

This Court in *Bull* as shown by the cases it cited, approved a theory of recoupment in which choice of forum or manner of proceeding does not affect the right to recoupment. In *Conner v. Smith*, a Mortgagor had recoupment against a Mortgagee who took personal property not mortgaged along with real property. The Court stated:

> "Shall this right be defeated, and the benefit of the exception to the Statute of Limitations be denied to the Complainants, because, instead of proceeding by bill, the election was made to foreclose by a sale under the power? . . . (C)an the circumstance of a mere difference in the modes by which the mortgagor is put to his defense, defeat and operate to deny the defense? We think not. It is very true, that the case does not come precisely within the letter of the law; but, it is also true, that such a defense in equity can never come precisely within the letter of a statute applicable by its terms to actions at law . . . So long as the contract, upon a breach of which the claim is predicated, subsists and may be enforced, the claim itself may be pleaded in reduction." 7 So. at 153

IV. THE MITIGATION PROVISIONS ARE COMPLEMENTARY AND DEAL WITH COMPLETELY DIFFERENT SITUATIONS.

The Government continues to claim that the mitigation provisions of the Internal Revenue Code (Sections

1311-1314) are the exclusive remedy when inconsistent positions of the Internal Revenue Service subject a Taxpayer to double taxation. This is despite the fact the mitigation provisions deal solely with income tax and would not have helped the Taxpayer in *Bull*.

The intent of Congress with regard to the mitigation provisions is set forth in S. Rep. No. 1567, 75th Cong. 3d Sess. 49 (1938)

> "The purpose of the statute of limitations to prevent the litigation of stale claims is fully recognized and approved. But it was never intended to sanction active exploitation, by the beneficiary of the statutory bar, of opportunities only open to him if he assumes a position diametrically opposed to that taken prior to the running of the statute. The Federal courts in many somewhat similar tax cases have sought to prevent inequitable results by applying principles variously designated as estoppel, quasi-estoppel, recoupment and set-off. For various reasons, mostly technical, these judicial efforts cannot extend to all problems of this type. Nor can they provide a uniform, systematic solution of these problems. Legislation has long been needed to supplement the equitable principles applied by the courts and to check the growing volume of litigation by taking the profit out of inconsistency, whether exhibited by taxpayers or revenue officials and whether fortuitous or the result of design.

Accordingly, it is clear no replacement of equitable recoupment by mitigation was intended, nor were the mitigation provisions intended to be exclusive. Indeed, Congress sanctioned the Court's application of recoupment.

That the Government seeks to use the statute of limitations in the precise manner disapproved of by Congress can be seen by considering the implications of their inconsistent positions to the Estate of Harold Schrier. The income or gift was received by Frances Dalm when she was serving as Administratrix of that estate. If it was not a gift, presumably the Estate would have been entitled to a deduction. If the deduction was granted, the Government would be treating the transfer as income in all instances except the Dalms' claim for refund of gift tax. If no deduction was granted, as we believe was the case, the Government is in the position of maintaining in each instance (with regard to estate tax, gift tax and income tax) that position (gift or executor's fee) that maximizes its tax receipts without regard to consistency or principle. The government should not be permitted to exploit, by the benefit of the statutory bar, opportunities only open to it if it assumes a position diametrically opposed to that taken prior to the running of the statute. This Court should take the profit out of the government's inconsistency by reaffirming its doctrine of equitable recoupment in the instant case. The Government seeks to make a profit taking inconsistent positions. The Government should be seeking respect and fairness in the equal administration of the tax laws, not the quick profits of a wall street trader.

V. THE HOLDING IN *DALM* IS NOT INCONSISTENT WITH THE THEORY OF STATUTES OF LIMITATION

The rationale of statutes of limitation as they relate to equitable recoupment is set forth in Andrews, *Modern-*

Day Equitable Recoupment and the "Two Tax Effect," Avoidance of the Statutes of Limitation in Federal Tax Controversies, 28 Ariz. L. Rev. 595, 645-646 (1986).

> "Given the foregoing reasons for the existence of tax limitation statutes, particularly that of preventing the litigation of stale claims, their relationship to the single transaction element of equitable recoupment and to the automatic facet of *Bull*, quickly becomes apparent. The Supreme Court seemingly imposed the single transaction element of the doctrine because it helps avoid the very staleness problem against which limitations are principally directed. Where a single item, transaction or taxable event is under scrutiny in connection with the open claims of one party, the facts of such transaction relating to the barred claim of the other party are, almost be definition, the same or related and substantially known. Consequently, the single transaction concept helps ensure a minimal staleness problem. Obviously in such a situation the negation of a statute of limitation by the application of equitable recoupment is more palatable.
>
> The same may be said of the automatic facet of *Bull* . . . The determination of the open claim leaves little or no factual issue with respect to the barred claim, and hence, no real problem of staleness exists. Unlike the justifiable fear voiced by the Court in *Electric Storage Battery*, here no search with respect to the barred claim is either invited or necessary as it is already automatically known."

The "automatic feature" of *Bull* is described at 644.

> "Another obvious, but unemphasized, feature of *Bull*, however, was the automatic nature of its conclusion with respect to the barred estate tax refund claim of the taxpayer once the Court made its determination as to the open income

> tax claim of the government (being litigated in the setting of the taxpayer's income tax refund suit). That is, once the court determined that the post-death partnership profits were properly subject to the income tax, it was pretty much automatic, in the circumstances of that case, that such profits had been improperly subjected to the estate tax."

With respect to the Government's claim that the decision below would undermine the goals of finality and repose, the following language at page 646 is particularly appropriate:

> "the concept of final repose also does not seem to be of overwhelming importance where the claim of one party may only be inchoate or not even exist until the determination concerning the open claim has occurred, at which time the former may already be barred."

In *Dalm* as in *Bull*, nothing is left to be determined on stale evidence. If it was a gift, it was not income. If it was income, it was not a gift. The Tax Court's decision gave rise to a circumstance (gift tax collected on income) that automatically required a recoupment or set-of.

The Government cites *Andrews* without regard to his more philosophical considerations simply for his footnote claim that *Kolom v. United States*, 791 F.2d 762 (9th Cir. 1986) is "incorrect." If *Kolom* is "incorrect" it does not follow that *Dalm* is incorrect. *Kolom* involved only income tax and the mitigation provisions applicable to income tax only may have been his exclusive remedy, unlike *Dalm* where a non-income tax is involved. *Kolom* also differs from *Dalm* in that it is not clear whether his claim was filed while the main action was pending, a factual issue not present in *Dalm*.

Nevertheless, it is clear that Andrews did not analyze *Kolom* rigorously in line with his own scholarly analysis of the rationale behind statutes of limitation. The statute of limitations is not undercut if the only time-barred claims affected are those "automatically" valid by a judicial determination of the nature of the transfer involved, a description which fits *Kolom*. If *Kolom* received the income in 1972, it is plain he did not receive it in 1973. No stale claim needed to be litigated. A Court had already held that no tax was owning on the income for 1973 because the income was held to have been received in 1972. In *Bull*, if it was corpus, it was not income. In *Dalm* if income, it was not a gift. When a court determined one it determined the other. Far from stale claims needing to be litigated, no claim needs to be litigated at all. All necessary issues have been determined. The Internal Revenue Service should have allowed the credit when it proceeded for income tax and is duty bound to refund the incorrect tax. Having neglected or refused to do so an action will lie to force compliance. Not only did the Court of Appeals do equity it followed a principal of fundamental fairness established by this Court the Government seeks to eliminate from tax administration.

CONCLUSION

The *Dalm* case has been rightly decided. Therefore, the decision of the Court of Appeals should be affirmed.

Respectfully submitted,

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